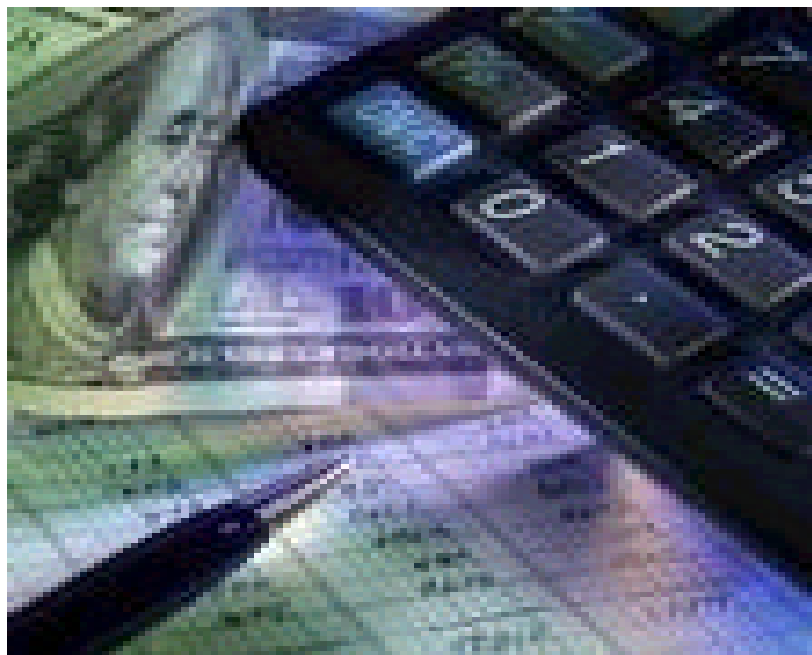




Internal Audit Report

Department of Finance
April 2002



Audit Team Members

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Internal Audit Department

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April 4, 2002

Don Stapley, Chairman, Board of Supervisors
Fulton Brock, Supervisor, District I
Andrew Kunasek, Supervisor, District III
Max W. Wilson, Supervisor, District IV
Mary Rose Wilcox, Supervisor, District V

We have completed our FY 2001-2002 review of the Department of Finance (DOF). The audit was performed in accordance with the annual audit plan that was approved by the Board of Supervisors.

The highlights of this report include the following:

- Two County clearing funds (Fund 746 and 767) hold an estimated \$884,540 in stale dated warrants and other funds that could be transferred to the County General Fund.
- Prompt payment discounts offered by County vendors are not consistently captured. This is primarily because County departments do not deliver payment voucher packets to Accounts Payable in time to earn the discounts. In an expenditure sample tested, 16% (\$4,600) of the available prompt payment discounts were not captured.

Attached are the report summary, detailed findings, recommendations, and DOF management's response. We have reviewed this information with the DOF Director and appreciate the excellent cooperation of DOF management and staff. If you have questions, or wish to discuss items presented in this report, please contact Joe Seratte at 506-6092.

Sincerely,

A handwritten signature in cursive script that reads "Ross L. Tate".

Ross L. Tate
County Auditor

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Executive Summary

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Two County clearing funds hold approximately \$885,000 in stale dated warrants and other funds that could be transferred to the County General Fund, as authorized by Arizona Revised Statutes (ARS). These monies have accumulated in the clearing funds since Fiscal Year (FY) 1996. The Department of Finance (DOF) is working with County Counsel to address related legal issues. DOF should reconcile clearing funds to identify all transferable monies and transfer stale dated warrants and other monies as appropriate to the County General Fund.

Lost Prompt Payment Discounts

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The County does not consistently capture prompt payment discounts offered by County vendors. Our testing of 207 FY 2002 invoices found 16 percent that reflected errors in applying prompt payment discounts. Additionally, DOF's "Discount Lost/Discount Taken Report" does not include all incidents of lost discounts. Seventeen of the 23 missed discounts identified in our testing do not appear on the report. Failure to capture prompt payment terms increases costs to the County comparable to paying a 37 percent annual interest rate.

Introduction

Background

The Department of Finance (DOF) oversees, reports, processes, and analyzes County financial transactions. DOF provides services to all County departments and various external users. The department is responsible for:

- Preparing the Comprehensive Annual Financial Report (CAFR) and Expenditure Limitation Reports
- Monitoring all real estate services including sales and leases of County real estate
- Reporting annual Form 1099 information to the IRS
- Setting the tax rates for the County, cities, schools, and special districts.

The Board of Supervisors (Board) appointed the first County Finance Director in January 1953 to coordinate all financing operations and report through the County Manager to the Board. DOF operates through the powers granted to the Board under Arizona Revised Statutes (ARS) 41-1346. The department must comply with various portions of Article 11 Chapter 4 promulgating financial provisions for the operation of the County. Additionally, several of DOF's external reporting mechanisms are federally mandated. These include:

- CAFR
- Single Audit Package and Management Letter
- Cost Allocation Document (Federal OMB Circular A-87 general requirements for charging indirect costs to grants)
- Bonded Indebtedness Report – (ARS 35-501)

DOF began fiscal year (FY) 2002 with 35 budgeted positions and then re-aligned projects. Since the second quarter of FY 2002, the department has operated with 33 budgeted positions. DOF is organized into two functional areas:

- Analysis, systems, and general ledger transactions - Monthly variance reports, journal vouchers, Advantage 2.0 maintenance, Report Web maintenance, cash management, property tax rate preparation, central service cost allocation, and data processing.
- General accounting, reporting and grants - Debt service, capital projects tracking, grant monitoring, lease financing, CAFR preparation, fixed assets maintenance, and accounts payable.

Mission and Goals

DOF's mission is to provide financial information and services to Maricopa County government so that they can effectively manage their resources. The department has established goals to:

- Develop procedures and implement processes to support Managing for Results and GASB 34.
- Obtain and maintain an employee turnover rate no greater than nine percent.
- Develop a Capital Improvement Project (CIP) financing plan and quarterly status reports to ensure that all financing is consistent with budgeting resources, favorable expenditure limitation outcomes, and cost effectiveness.
- Improve customers' ability to manage results through enhancement and full utilization of the existing financial system, which will provide customized real time information.

Scope and Methodology

Our Audit objectives were to determine if:

- Suspense, clearing, and other fund accounts include monies that should be transferred to the County General Fund or escheated to the State.
- The process of identifying and capturing all available vendor discounts is being optimized.
- Effective internal controls over the accounting and monitoring of Fixed Assets have been established and are exercised.
- Established controls are adequate to identify accurate sales tax applications.

The audit was performed in accordance with Government Auditing Standards.

Sales Tax and Fixed Assets

During audit planning and fieldwork activities, Internal Audit found little risk related to the County's payment of sales tax on vendor invoices. The burden of sales tax payment (technically a Transaction Privilege Tax) falls on the vendor. Under or uncharged sales tax must be paid by the vendor and does not represent a County liability.

We also performed a high level review of the Fixed Asset cycle, identifying control weaknesses in the recording of asset location and asset disposition through surplus. Further testing outside of the scope of the DOF audit will be performed in a subsequent engagement on Countywide fixed asset activities.

**Related Issues
Identified**

During our review of suspense and clearing funds, we identified a Maricopa Integrated Health System (MIHS) warrant clearing fund, through which all non-payroll warrants for the health system are processed. We found that MIHS has not addressed stale dated warrants in the fund (Fund 567) since prior to calendar year 1997. MIHS is reviewing its stale dated warrant procedures and seeking County Counsel direction on the appropriate methodology for transferring stale dated warrants and other funds.

Department Reported Accomplishments

DOF has provided Internal Audit with the following information to be included in this report.

- The Finance Department was actively involved in the preparation of the following two components associated with the Governmental Performance Project:

Financial Management - Overall Grade A-
Capital Management - Overall Grade B+

- The Finance Department participated in the voluntary budget balancing plan and managed to reduce our annualized budget by over \$107,000 or 5.2% of our base annual budget. This reduction included effectively re-aligned projects and duties to eliminate two of our budgeted positions.
- During January of 2002, the Department of Finance took advantage of low interest rates and refunded outstanding Maricopa County General Obligations, saving more than \$750,000. It is anticipated that \$1.2 million will be saved during May 2002 with the refinancing of several capital leases.
- The Finance Department Employee Satisfaction Survey results showed higher ratings in almost each area. The overall composite score went from 5.32 in 00-01 to 5.78 in 01-02. The survey was conducted in January and results were shared with all department employees during February.
- The Finance Department successfully implemented Managing for Results without the need for either internal or external consultants. 100% of the functions associated with MFR were absorbed into the current structure.
- The Finance Department is currently implementing Governmental Accounting Standards Board #34 to proactively address the demand for government accountability. Although many other governmental entities have utilized the services of consultants and accounting firms, our department is effectively implementing it utilizing our own existing staff.
- The Finance Department is in the process of evaluating county-wide collections efforts. During February 2002, the Superior Court Collections unit was moved to the Department as part of this initiative. Ongoing efforts in this area should prove to be productive for the County as a whole and will capitalize on the relationship between the Department of Finance and the County Court System.
- The activity based cost accounting model (PAS Costing) needed to support the County's Managing for Results (MFR) program has been fully developed, tested and implemented into the County's General Ledger system. This was done utilizing the existing general ledger accounting system with out the need for customization.
- The Department of Finance evaluated reporting needs and selected InfoAdvantage as its reporting tool. This product will provide a state of the art tool for extracting data for reporting purposes from the general ledger system.

Issue 1 Suspense Account Monitoring

Summary

Two County clearing funds hold approximately \$885,000 in stale dated warrants and other funds that could be transferred to the County General Fund, as authorized by Arizona Revised Statutes (ARS). These monies have accumulated in the clearing funds since Fiscal Year (FY) 1996. The Department of Finance (DOF) is working with County Counsel to address related legal issues. DOF should reconcile clearing funds to identify all transferable monies and transfer stale dated warrants and other monies as appropriate to the County General Fund.

Stale Dated Warrants

Warrants issued by County agencies are paid through a series of clearing funds. The largest clearing fund is Fund 767, which is used for the majority of warrants drawn on the County General Fund.

Outstanding warrants are deemed “stale” one year after the date of issuance. ARS 11-644 directs DOF to notify, in writing, the holder of all stale dated warrants that the warrant is void. Stale dated warrant holders have an additional year to make a claim to the County for the amount of the warrant. As per ARS authority, the dollars represented by stale dated warrants are then available for use in the County General Fund.

Approximately \$300,000 Available to County General Fund

We found that stale dated warrants have not been moved from Fund 767 to the County General Fund since 1996. Up to \$300,000 of accumulated stale dated warrants currently resides in the fund. These dollars are available and may be used to increase the County General Fund.

Fund 767 should have a detailed reconciliation to ensure warrants represent valid transactions and the fund is clear of processing errors such as duplicate warrants, unrecorded voids, or other types of errors. DOF has not recently performed a detailed reconciliation of Fund 767.

Other Funds Available

Maricopa County Justice Courts routinely receive bond and restitution monies that cannot be remitted to their rightful owners. In accordance with the requirements of ARS 22-116, Justice Courts maintain a fund (Fund 746) with the County Treasurer’s Office that is used primarily to hold these monies. The payee may claim these monies for another year. After that year, all money remaining in the suspense account may be deposited in the County General Fund.

The Arizona Department of Revenue (DOR) recently conducted an audit and identified \$584,539 in other funds in Fund 746, dating back to the 1980’s. The DOR audit maintains that these amounts should be escheated to the State. DOR is also assessing the County approximately

\$313,000 in interest related to the funds.

The County Attorney's Office contends that the monies identified within the audit should remain with the County, following ARS guidelines, and can be transferred to the County General Fund. The County Attorney's Office is requesting a hearing with DOR to resolve the issue.

Effect on County

The \$885,000 identified as transferable monies in Funds 767 and 746 continues to earn interest with the Treasurer. However, these resources are not available for use in County operating activities until they are transferred to the County General Fund. The DOR audit also illustrates that if timely transfers are not made, the County is exposed to potential assessments from the State.

Recommendation

DOF should:

- A. Perform a detailed reconciliation of Fund 767 and transfer appropriate monies to the County General Fund.
- B. Upon completion of the DOR legal process, transfer \$584,539, or other appropriate amount, to the County General Fund.

Issue 2 Lost Prompt Payment Discounts

Summary

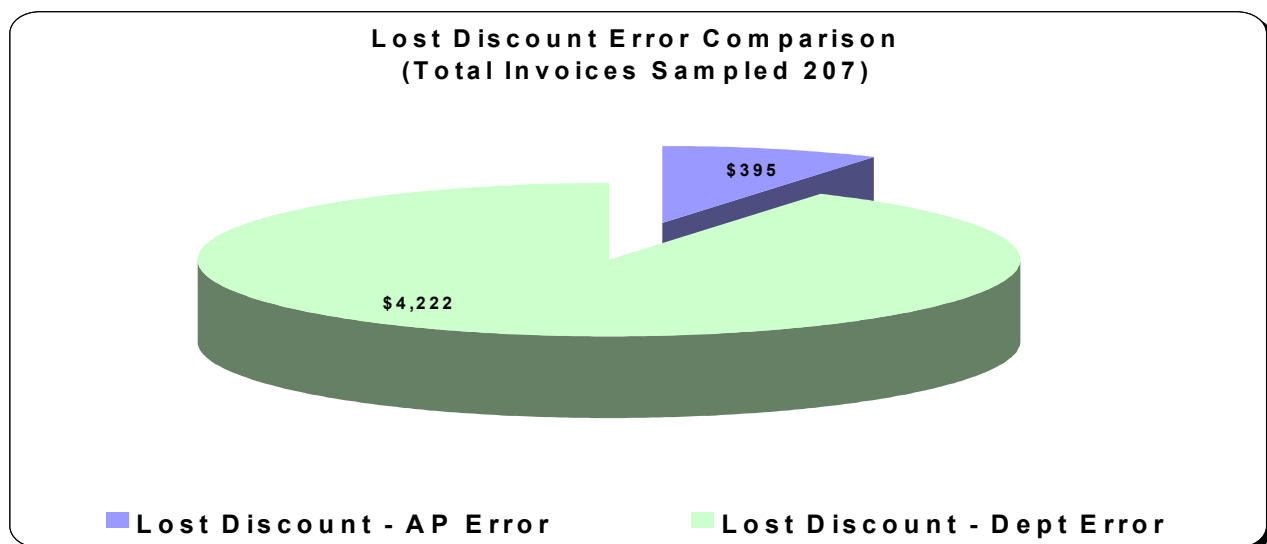
The County does not consistently capture prompt payment discounts offered by County vendors. Our testing of 207 FY 2002 invoices found 16 percent that reflected errors in applying prompt payment discounts. Additionally, DOF's "Discount Lost/Discount Taken Report" does not include all incidents of lost discounts. Seventeen of the 23 missed discounts identified in our testing do not appear on the report. The failure to capture prompt payment discounts increases costs to the County comparable to paying a 37 percent annual interest rate.

Prompt Payment Discount

The County has made a priority of taking all available prompt payment discounts offered by vendors. DOF produces a report ("Discount Taken/Discount Lost Report") to help identify missed prompt payment discounts. To determine how well County departments capture prompt payment discounts, we reviewed 207 invoices. We found 23 (11%) instances where discounts were missed. Two types of errors, resulting in lost prompt payment discounts, were identified:

- Payment voucher packets were not delivered to DOF Accounts Payable (A/P) in time to capture the discounts offered (91%).
- Voucher packets were not processed timely by A/P (9%).

The chart below depicts the dollar amount and source of lost discounts.



We also noted instances where the County took unearned prompt payment discounts (e.g., discounts applied to invoices paid late or commodities not eligible for discount).

**Discount Report
Verification**

We examined DOF's lost discount report to verify its accuracy. We found that 17 (74%) of the 23 missed discounts, identified in our testing, were not reported. These exceptions were the result of the originating departments' failure to identify available discounts on the payment voucher packets. Since this is the largest segment of lost discounts observed in our sample, the lost discount report may substantially understate missed discounts.

Impact on County

Estimating the full impact of missed discounts is difficult because not all available discounts are identified in the Advantage 2.0 system. However, the Materials Management Department reports that the County has approximately 64 vendors that offer prompt payment discounts. Purchases from these vendors during FY 2001 totaled approximately \$5.4 million. If the County had taken advantage of all available discounts, approximately \$99,000 could have been saved. A greater emphasis on negotiating prompt payment terms during future contract cycles could substantially increase these potential savings.

Recommendation

None, for information only.

NOTE: Departmental prompt payment discount issues will be incorporated in Internal Audit's upcoming Control Self-Assessment Workshop for Disbursements and Payables.

Department Response

**AUDIT RESPONSE
DEPARTMENT OF FINANCE
March 29, 2002**

Issue #1:

Two County clearing funds hold approximately \$885,000 in stale dated warrants and other funds that could be transferred to the General Fund, as authorized by Arizona Revised Statutes (ARS). These monies have accumulated in the clearing funds since Fiscal Year (FY) 1996.

Response: Concur. The Arizona Department of Revenue (DOR) has asserted that the monies in one of the funds should be remitted to DOR as unclaimed property. The Department of Finance and County Counsel believe the funds should not be considered unclaimed property and should be transferred to the General Fund. We are currently in the process of resolving the issue with the assistance of County Counsel.

Recommendation A:

Perform a detailed reconciliation of Fund 767 and transfer appropriate monies to the General Fund.

Response: Concur. Reconciliation is in process and transfer will be made upon completion.

Target Completion Date: 6/30/02

Benefits/Costs: Appropriate treatment of stale dated warrants and compliance with Arizona Revised Statutes.

Recommendation B:

Upon completion of the DOR legal process, transfer \$584,539, or other appropriate amount, to the General Fund.

Response: Concur.

Target Completion Date: Contingent upon completion of DOR legal process.

Benefits/Costs: Appropriate treatment of County funds and compliance with Arizona Revised Statutes.


Issue #2:

The County does not consistently capture prompt payment discounts offered by County vendors. Our testing of 207 FY 2002 invoices (\$1.5 million total) found 16 percent that reflected errors in applying prompt payment discounts. Additionally, DOF's "Discount Lost/Discount Taken Report" does not include all incidents of lost discounts. Seventeen of the 23 missed discounts identified in our testing do not appear on the report. Failure to capture prompt payment terms increases costs to the County comparable to paying a 37 percent annual interest rate. If the County had taken advantage of all available discounts, approximately \$99,000 could have been saved. A greater emphasis on negotiating prompt payment terms during future contract cycles could substantially increase these potential savings.

Recommendation : None, for information only.

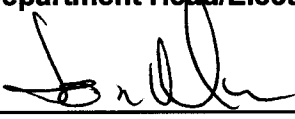
Response: The capture of prompt payments discounts is a countywide manner and success in this area is contingent on departmental involvement and responsibility. We will gladly participate and assist with Internal Audit's upcoming Control Self-Assessment Workshop for Disbursements and Payables. In addition, we will continue our training and monitoring in this area as well.

Approved By :



Department Head/Elected Official

3-29-02
Date



Chief Officer

3-29-02
Date



County Administrative Officer

3/29/02
Date